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**THREE SACRAMENTANS CONVICTED IN HUGE  
TAX FRAUD, INVESTMENT FRAUD AND  
MONEY LAUNDERING SCHEME**

**Among the losses caused by defendants' mail and wire fraud conspiracy was over \$235,000 from a church, resulting in loss of their entire building fund**

SACRAMENTO--United States Attorney John K. Vincent and Victor S.O. Song, IRS Special Agent in Charge for Northern California, announced today that HERBERT ARTHUR BATES, age 70, of Sacramento, DAVID LARRY SMITH, age 58, of Auburn, CA, and CHRISTOPHER R. BATES, age 43, also of Sacramento, were convicted this morning after an eight week jury trial of conspiracy to defraud the United States by impairing and impeding the Internal Revenue Service in the assessment and collection of income taxes, conspiracy to engage in mail and wire fraud and conspiracy to engage in money laundering. Sentence will be imposed by the Honorable Morrison C. England, Jr., United States District Judge, on June 3, 2003.

DAVID LARRY SMITH was convicted of 108 counts of conspiracy, tax fraud, mail fraud, wire fraud and money laundering. In addition to the three conspiracy counts, SMITH was convicted of 21 counts of aiding and assisting taxpayers to file false tax returns, 26 counts of mail fraud, 7 counts of wire fraud, and 51 counts of money laundering. The maximum penalty which SMITH faces is imprisonment for 1,158 years, a fine of \$27,000,000, a term of supervised release and a special assessment of \$10,800.

In addition to the three conspiracy counts, HERBERT BATES was convicted of 21 counts of aiding and assisting taxpayers to file false tax returns. The maximum penalty which HERBERT BATES faces is imprisonment for 88 years, a fine of \$6,000,000, a term of supervised release and a special assessment of \$2400.

CHRISTOPHER BATES, the son of defendant HERBERT BATES, was convicted of three conspiracy counts. The maximum penalty which CHRISTOPHER BATES faces is imprisonment for 30 years, a fine of more than \$2 million, a term of supervised release, and a special assessment of \$300. CHARLOTTE WADSWORTH, age 62, also of Sacramento, was acquitted of conspiracy to defraud the United States by impairing and impeding the Internal Revenue Service in the assessment and collection of income taxes, which was the only count with which she was charged.

According to Assistant United States Attorneys Robert M. Twiss and Douglas Sprague, who prosecuted the case, the evidence presented at trial proved that the defendants sold a form of trust, which they called an Unincorporated Business Organization (“UBO”), to approximately 249 investors. The defendants charged between \$3,000 and \$7,500 for the creation of these UBO’s. DAVID LARRY SMITH and HERBERT BATES advised clients that they could transfer all of their income and assets to the UBO, and after transferring their income and assets, the clients no longer had to file individual income tax returns nor pay federal income taxes.

DAVID LARRY SMITH and HERBERT BATES advised clients that they could “deduct” virtually all payments by the UBO from the revenues which it received as a result of the transfers of income and assets by the clients. HERBERT BATES and DAVID SMITH told clients that they could deduct mortgage payments, rent, food, automobile expenses, and even haircuts from the revenue received by the UBO. HERBERT BATES and DAVID SMITH advised clients that so long as the UBO did not have more than a nominal amount of money in its bank account as of December 31st, the UBO also did not have to file a tax return nor pay any federal income taxes.

DAVID SMITH told clients that they could ensure that the UBO didn’t have more than a nominal balance in its bank account on December 31st by making either periodic or year ending “distributions” to the defendants, who operated in Sacramento under the names of the Guardian Group, the Joinder Group, Peer Financial Group, Aloha Leasing, the Keyus Group, International Management Services, PL Services, and Oscar 281B. The defendants also operated under the names of Le Caraibi Connessione Internazionale (“LCCI”) and the Andres Corporation, both of which were incorporated in the Cayman Islands.

DAVID SMITH told clients that they would return the “distributions” to the clients after the beginning of the new tax year in a form which gave the appearance of being from a non-taxable source. Among the ways in which defendants offered to return the money were by making a “loan” to the client’s UBO from a foreign bank or other foreign entity.

Another way in which SMITH offered to return the distributions was to provide the client with a credit card issued by a bank in the Cayman Islands. The clients could purchase goods and services with the card, and the bills would be paid by the Cayman Islands bank with money from the distribution. Accordingly, there would be no paper trail back to the UBO or the client here in the United States. In return for providing this service, the defendants charged the clients a fee of 10% to 11%.

The jury found that HERBERT A. BATES and DAVID L. SMITH used this scheme to aid and assist clients to file tax returns which were false because they either under reported income or over reported deductible expenses. HERBERT BATES and DAVID SMITH were convicted of 21 such counts involving approximately 10 taxpayers.

The jury found that HERBERT BATES, DAVID SMITH and CHRISTOPHER BATES engaged in a conspiracy to commit mail and wire fraud to defraud investors. Essentially, HERBERT BATES, DAVID SMITH and CHRISTOPHER BATES simply kept a substantial amount of the distributions made by clients, and DAVID SMITH made false statements and representations to clients to explain why the money could not be returned.

The evidence presented at trial established that defendant SMITH used a number of “lulling letters” sent to clients to cause them to falsely believe that their investments were safe, were appreciating in value, and would be available when they wanted the money returned. Instead of each client having a segregated account in which only his or her money was being held, however, the jury found that all clients funds held to support the credit card return option were in one account, and all holders of credit cards were making purchases against the one commingled account. Most clients lost most of the money which they thought they had on deposit. Some investors received small monthly payments of \$150 to assist in creating the false sense of security.

Among the victims of the investment fraud was the Christian Life Fellowship ("CLF") of Quincy, CA, whose board of trustees was told by DAVID SMITH that if the church placed its building fund of \$235,000 with Smith, Smith would guarantee an annual return of over 10% on an investment in a bank account or some other instrument for which there was no risk of loss. The church wire transferred \$235,000 to an account in the Cayman Islands at the direction of SMITH. CLF not only did not receive its annual gain of over 10% as promised by SMITH; CLF lost its entire building fund.

The evidence presented at trial proved how HERBERT BATES, DAVID SMITH and Lonnie Schmidt went to the Cayman Islands and met with a Cayman Islands banker to open bank accounts there and form Cayman corporations for use in the schemes to defraud. The evidence presented at trial established that DAVID SMITH and CHRISTOPHER BATES used these accounts to wire transfer client and investor money between Sacramento, an account at Credit Suisse Bank on the Isle of Guernsey in the Channel Islands of the United Kingdom, and accounts at Guardian Bank and Trust, Cayman Islands, in Georgetown, Grand Cayman in furtherance of the scheme to defraud. The evidence proved that many of these transfers were done with the intent to conceal the nature, source, location and control over the monies, and SMITH was convicted of 22 such money laundering counts.

In response to the verdicts, Victor S.O. Song, Special Agent in Charge, IRS Criminal Investigation, stated, "The conviction of these defendants today sends a strong message that the Internal Revenue Service will vigorously pursue charges against individuals who conspire to defraud the United States and attempt to launder proceeds of their illegal activity."

This case is the product of an extensive investigation by the Criminal Investigation Division of the Internal Revenue Service.

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